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JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 828

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,

Petitioner,

—against—

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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THE COURT PRESS, 130 Cedar Street, N. Y. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No.

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,

Petitioner,

—against—

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,

Respondents.

PETITION FOR WRIT OF CERTIORARI

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Norman Howard, a stockholder of Circle Wire & Cable Corporation, acting on behalf of himself and other stockholders of said corporation, respectfully prays for the issuance of a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit entered herein December 10, 1956, affirming the judgment of the United States District Court dismissing his complaint.

Opinions Below

The opinion of the District Court is reported 140 F. Supp. 507 and appears in Appellant's Appendix in the Court of Appeals 17a-27a. The opinion of the Court of Appeals is reported 238 F. 2d 790, and is appended to this petition pp. 19-27, *infra*.

Grounds of Jurisdiction

The opinion and judgment of the Court of Appeals is dated November 13, 1956 (*infra*, p. 28). Petition for rehearing was timely filed and denied by order dated December 10, 1956 (*infra*, p. 35). The jurisdiction of this Court is invoked under 28 U. S. C. §1254(1).

Questions Presented for Review

1. Did the Federal District Court have jurisdiction, as of a case arising under the laws of the United States, pursuant to 28 U. S. C. §1331 and 15 U. S. C. §78aa, of a stockholders derivative action to enjoin or set aside the voting of proxies ratifying the sale by a corporation of substantially all its assets when the necessary votes in favor of such sale were obtained in violation of the proxy regulations adopted pursuant to Section 14(a) of the Securities Exchange Act of 1934?

2. May a corporation enjoin or set aside a transaction effected by the violation of Section 14(a) of the Securities Exchange Act of 1934?

3. Did the Court of Appeals err in refusing to pass on the question whether an individual or class stockholders action to enjoin or set aside such transaction (which the District Court found to exist) was lost by failure to make timely application for a temporary injunction on the ground that the complaint alleging the relevant facts was not cast in the form of such an action, when:

(a) the complaint set forth the facts upon which relief could be granted, and

(b) the District Court had held that he would have granted leave to amend the complaint to properly present an individual or class action except for the fact that such an amended complaint would have been barred by such failure to make timely application for a temporary injunction.

Statutes and SEC Rule Involved

28 U. S. C. §1331:

> "The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $3000 exclusive of interest and costs, and arises under the Constitution, laws or treaties of the United States."

Securities Exchange Act of 1934, Section 27, as amended, 15 U. S. C. §78aa:

> "The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and

actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. * * *"

Securities Exchange Act of 1934, Section 14(a), 15 U. S. C. §78n(a):

"(a) It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national securities exchange or otherwise to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered on any national securities exchange in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule X-14a-9 (17 Code Fed. Reg. §240.14a-9) promulgated pursuant to Sec. 14(a):

"False or misleading statements. No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting, or other communication written or oral containing any statement which at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading."

Statement

Petitioner below sued "on behalf of himself and other stockholders of Circle Wire & Cable Corporation" (3a)*, (Circle) to enjoin the consummation of, or set aside if consummated *pendente lite*, a contract of sale by Circle of substantially all its assets.

After formal allegations, the complaint set forth the execution by Circle of a contract to sell to Cerro de Pasco Corporation (Cerro) all its assets, property and business except goodwill for $20,250,000 (par. 9, 6a), which contract by virtue of Section 20 of the New York Stock Corporation Law required the approval of holders of two-thirds of Circle's shares (par. 9, 7a); that Circle, whose stock was registered upon a national securities exchange, was subject to the proxy regulations of Section 14(a) of the Securities and Exchange Act of 1934 and Rule X-14a-9 prescribed thereunder which forbids solicitation of proxies by any statement "which at the time and in the light of the circumstances under which it is made is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading" (par. 10, 7a); that the individual defendants, who were officers and directors of Circle (par. 4, 4a), caused Circle to send to its stockholders through the mails and by instrumentalities of interstate commerce a notice of meeting and a proxy statement wherein the management solicited the proxies of the stockholders in favor of such sale (par. 11, 7a-8a); that such proxy

* References a are to Appellant's Appendix in the Court of Appeals.

statement was false and misleading in understating the inventory of Circle by more than $8,000,000 and similarly understating the earnings of Circle for the years 1952, 1953 and 1954 and the first nine months of 1955 (pars. 12, 13 and 14, 8a-10a), and was further misleading in failing to disclose that certain named dominant directors had a personal motive for the sale, i. e., by sale of the assets in bulk to reduce or eliminate the danger of discovery of the past understatement of assets and earnings which had been made to stockholders, the Securities and Exchange Commission and the Bureau of Internal Revenue (pars. 14f, 15 and 16, 10a-11a).

The prayer for relief was that the defendants be enjoined from voting such proxies; that they be declared void; and that the sale, if consummated *pendente lite,* be declared void and be cancelled and rescinded, and for alternative relief (13a).

The complaint was filed November 23, 1955. Service was made on Circle and Cerro and certain of the individual defendants before the meeting which was held November 28 (15a). At such meeting the proxies were voted and the sale approved and consummated on December 1, 1955 (14a, 15a).

Thereafter defendants moved to dismiss for want of jurisdiction. The question presented was whether the court had jurisdiction, under 28 U. S. C. §1331 and 15 U. S. C. §78aa, *supra,* pp. 3, 4, of the claim for relief presented; and, on the merits, whether Section 14(a) of the Securities and Exchange Act which, with the rule adopted thereunder, made unlawful the solicitation of the proxies in question but did not ex-

pressly give a private remedy for violation of such statute, nevertheless implied such a remedy. The District Court held that this section did not create any right of action on behalf of the corporation, the sale of whose assets was made possible by the illegally obtained proxies, but did create a right of action on the part of its stockholders of which the court had jurisdiction (23a); that the stockholders' right was limited to forcing the corporation to correct the false proxy statement and enjoining the holding of a meeting until such correction was made; but that plaintiff, in failing to seek a temporary injunction to postpone the meeting, was guilty of laches and was not now entitled to relief* (25a).

Accordingly the Court dismissed the complaint. This dismissal was ostensibly for lack of jurisdiction over the subject matter (17a); but such dismissal was, as above shown actually on the merits, i. e., the defense of laches (25a). The difference of course is vital; for if the complaint stated a claim based on federal law, which was substantial and not frivolous even though held not meritorious in law, the Court had jurisdiction to decide the action on common law grounds arising from the facts set forth in the complaint—breach of fiduciary duty, fraud and waste of corporate assets (pars. 18-20, 11a-12a)—even assuming that it eventually determined the federal grounds of the complaint

* The District Court construed the complaint as setting forth only a derivative and not a representative action. This, we believe, was error, for reasons mentioned infra, p. 14. However, this error was not prejudicial at the District Court level because the District Court said that he would have granted leave to amend but for the fact that laches made such amendment futile (25a).

to be without merit. *Bell* v. *Hood,* 327 U. S. 678; *Hurn* v. *Oursler,* 289 U. S. 238.

On appeal plaintiff argued that federal jurisdiction existed as noted. Furthermore, on the merits he argued that Section 14(a) of the Securities Exchange Act of 1934 and Rule X-14a-9 adopted thereunder gave a cause of action both to the corporation and to the stockholders; and that the stockholders' action had not been lost for laches in failing to ask for a temporary injunction in view of the well settled rule that one who proceeds in the face of a prayer for permanent injunction acts at his peril and must restore the *status quo* if he loses on the merits. *Wingert* v. *First National Bank of Hagerstown,* 223 U. S. 670, 672; *Jones* v. *Securities and Exchange Commission,* 298 U. S. 1, 16-18; *Subin* v. *Goldsmith,* 2 Cir., 224 F. 2d 753, 761, 762.

The Court of Appeals affirmed. (Judges Medina, Learned Hand and Hincks, per Medina, J.) It held (1) that Section 14(a) and Rule X-14a-9 did not afford a substantive right to the corporation (pp. 24, 25, *infra*); (2) that since the complaint was "unequivocally cast in terms of the rights of the corporation" and was neither an individual nor a representative action by or on behalf of stockholders they need not determine whether the statute and rule might be construed as creating substantive rights on behalf of stockholders as individuals (p. 25, *infra*); (3) that there was no federal jurisdiction because plaintiff's claim was for violation of state created rights and was "in no real or substantial sense dependent upon the provisions of the Securities and Exchange Act of 1934 relative to proxy statements" (pp. 26, 27, *infra*).

In so deciding the Court stated that it was applying the test of *Gully* v. *First National Bank in Meridian,* 299 U. S. 109 (p 26, *infra*). It further held that there was no pendent jurisdiction under *Hurn* v. *Oursler,* 289 U. S. 238 (p. 27, *infra*).

The opinion made no mention of the holding of the lower court that plaintiff as a stockholder had a right grounded in federal law which he could have asserted as an individual or class representative had he not lost this right by failure to apply for a temporary injunction to restrain the holding of the meeting. By petition for rehearing plaintiff called the court's attention to the fact that in failing to review the District Court's holding on this point on the ground that the complaint did not properly present an individual or class stockholders action they were in effect denying him the right to amend which the District Court would have granted had he not been of the opinion that such amendment would be futile on account of laches, thus denying his right to review the holding below on the point of laches (pp. 32-34, *infra*). The Court denied the petition without further expression of opinion (p. 35, *infra*).

REASONS FOR GRANTING THE WRIT

I

The Court of Appeals, in holding that there was no federal jurisdiction of a complaint based on violation of a federal statute, has decided an important question of federal law in a way probably in conflict with applicable decisions of this Court.

1. The leading modern case is *Bell* v. *Hood,* 327 U. S. 678. It was there decided (p. 681) that "where

the complaint, as here, is so drawn as to seek recovery directly under the Constitution or laws of the United States, the federal court, but for two possible exceptions later noted, must entertain the suit. * * *" The Court continued, pp. 682, 683:

> "Jurisdiction, therefore, is not defeated as respondents seem to contend, by the possibility that the averments might fail to state a cause of action on which petitioners could actually recover. For it is well settled that the failure to state a proper cause of action calls for a judgment on the merits and not for a dismissal for want of jurisdiction. Whether the complaint states a cause of action on which relief could be granted is a question of law and just as issues of fact it must be decided after and not before the court has assumed jurisdiction over the controversy. If the court does later exercise its jurisdiction to determine that the allegations in the complaint do not state a ground for relief, then dismissal of the case would be on the merits, not for want of jurisdiction. *Swafford* v. *Templeton,* 185 U. S. 487, 493, 494; *Binderup* v. *Pathe Exchange,* 263 U. S. 291, 305-308. [Footnote omitted.] The previously carved out exceptions are that a suit may sometimes be dismissed for want of jurisdiction where the alleged claim under the Constitution or federal statutes clearly appears to be immaterial and made solely for the purpose of obtaining jurisdiction or where such a claim is wholly insubstantial and frivolous. The accuracy of calling these dismissals jurisdictional has been questioned. *The Fair* v. *Kohler Die Co., supra,* 228

U. S. at 25. But cf. *Swafford* v. *Templeton, supra.*"*

Hurn v. *Oursler,* 289 U. S. 238, 246, holds that if federal jurisdiction exists but the federally based claim is dismissed for lack of merit in fact or law the court retains jurisdiction to try the case on any common law grounds arising from the same facts. The combination of *Bell* and *Hurn* has recently been reiterated in *Montana-Dakota Utilities Company* v. *Northwestern Public Service Company,* 341 U. S. 246. Here the Court of Appeals had dismissed for want of jurisdiction a suit brought under Section 317 of the Federal Power Act which confers on District Courts of the United States "exclusive jurisdiction of violations of this Act or the rules, regulations and orders thereunder and of all suits in equity and actions at law brought to enforce any liability or duty created by, or to enjoin any violation of, this Act or any rule, regulation or order thereunder" (p. 257). This is substantially the language granting federal courts exclusive jurisdiction of actions arising under the Securities and Exchange Act, 15 U. S. C. 78aa, *supra,* p. 4. The majority and minority

* It cannot be seriously contended that the federal claim here asserted is insubstantial or frivolous. In *Subin* v. *Goldsmith,* 2 Cir., 224 F. 2d 753, 766, Judge Frank expressed the opinion that a violation of proxy regulations gave rise to a federally based cause of action on behalf of a corporation to set aside corporate action approved by proxies secured in violation of Section 14(a), citing *Goldstein* v. *Grosbeck,* 2 Cir., 142 F. 2d 422; *Fischman* v. *Raytheon Manufacturing Company,* 2 Cir., 188 F. 2d 783; *Baird* v. *Franklin,* 2 Cir., 141 F. 2d 238; *Fratt* v. *Robinson,* 9 Cir., 203 F. 2d 627; and *Remar* v. *Clayton Securities Corporation,* (D. C.), 81 Fed. Supp. 1014, 1017; to which list may be added *Fitzgerald* v. *Pan American World Airways, Inc.,* 2 Cir., 229 F. 2d 499, subsequently decided. The majority, Judges Medina and Brennan, expressed doubt as to the existence of a corporate cause of action but decided the case on other grounds, 224 F. (2d) at p. 774.

of this Court agreed, at pp. 249 and 259, that federal jurisdiction existed irrespective of the Court's determination of the merits of the action.*

2. In the instant case the Court of Appeals went off on the point that since the complaint stated a cause of action good at common law for rescission on account of fraud and breach of fiduciary duty "the allegations with reference to the proxy statement constitute a mere excrescence or superfluity tacked on to what are otherwise sufficient allegations of a claim for relief under New York Law" (*infra*, p. 27).

However, the fact that a wrong is actionable under state law does not prevent its being actionable under federal law. *Bell* v. *Hood*, 327 U. S. 678, 680, 681; cf. *Fitzgerald* v. *Pan American World Airways*, 2 Cir., 229 F. (2d) 499; *Fielding* v. *Allen*, 2 Cir., 181 F. (2d) 163. Many of the cases arising under the federal securities acts involve an element of fraud or breach of fiduciary duty; but this has not been thought to oust federal jurisdiction. Cf. *Deckert* v. *Independence Shares Corp.*, 311 U. S. 282. Accordingly, the existence of a "common law cause of action based on misuse of powers by directors of a controlled corporation . . . does not preclude the existence of the same circumstance from giving rise to a cause of action that has its roots in" a federal statute. Frankfurter, J., dissenting in *Montana-Dakota Utilities Company* v. *Northwestern Public Service Company*, 341 U. S. 246, at p. 259.** Thus when a cause of action in a federal court is based on equally valid federal and non-federal

* The Court divided on the point whether the relief requested was the kind of relief which courts, as distinguished from commissions, were equipped to give. Obviously no such question exists in this case.

** The majority did not differ on this point.

grounds, it is pertinent to inquire which grounds, if either, are "a mere excrescence or superfluity".

3. The Court of Appeals in holding that the common law grounds were basic and the federal grounds superfluous relied on certain language in *Gully* v. *First National Bank in Meridian,* 299 U. S. 109 (*infra,* p. 26). But *Gully* was not a case where the complaint was based on state and federal grounds. The right asserted—to tax shares in a national bank—was based on state law only; and the question of federal law—whether the United States had assented to the tax—was not a basis of the asserted right, and might or might not be raised by way of defense. According to this Court, *Gully* stands for the well-settled proposition that federal jurisdiction, based on the assertion of a federal right, must appear from the face of the complaint. As this Court said in *Payton* v. *Railway Express Agency, Inc.,* 316 U. S. 350, 353, citing *Gully:* "Whether a suit arises under a law of the United States must appear from the plaintiff's pleading not the defenses which may be interposed to, or be anticipated by it. Petitioner's pleading, which we have summarized, satisfies this requirement, since it adequately discloses a present controversy dependent for its outcome upon the construction of a federal statute." See also *Skelly Oil Company* v. *Phillips Petroleum Company,* 339 U. S. 667, 672.

Where, as in the instant case, the complaint rests on both state and federal grounds, *Gully* is satisfied. The rule of *Bell* v. *Hood,* 327 U. S. at p. 681, that "the party who brings the suit is master to decide what law he will rely on" then comes into play; and if plaintiff says that he relies on federal law the case presented is within the federal jurisdiction.

II

The Court erred in refusing to pass on the question whether the complaint, considered as an individual or class action, was barred by laches on the ground that it was not cast in the form of such an action, when the District Court had held that he would permit this alleged defect to be cured by amendment had he not considered that an amended complaint would have been barred by laches.

Petitioner does not concede that his complaint required amendment to make it an individual or class action.* However, it is immaterial whether or not the complaint required amendment because the District Court held that he would have granted leave to amend had he not considered such leave to be futile

* If labels are important, petitioner attached the proper label when he alleged that he sued "on behalf of himself and other stockholders of Circle Wire and Cable Corporation". (3a) But labels are no longer important. Rule 8(a)(2) F. R. C. P. requires that the complaint contain only "a short and clear statement of the claim showing that the pleader is entitled to relief." This means any relief, including without limitation the relief to which plaintiff thought he was entitled. This is so even though the Court has to pick a few relevant allegations out of a rambling, inartistic complaint. *Dioguardi* v. *Durning*, 2 Cir., 139 F. 2d 774, 775. The effect and purpose of the Rule was to do away with "theory of the case" pleading, 2 Moore Fed. Prac. 1656-7; and it becomes the Court's duty to "grant the relief to which prevailing party is entitled whether demanded or not." *Gins* v. *Mauser Plumbing Supply Co.*, 2 Cir., 148 F. 2d 974, 976. And the complaint should not be dismissed for insufficiency "unless it appears a certainty that plaintiff is entitled to no relief under any set of facts which could be proved in support of the claim." 2 Moore Fed. Prac. 2245, cited by Judge Medina in *Forstmann Woolen Co.* v. *Murray Sices Co.*, 10 F. R. D. 367, 370. Hence, without amendment this Court should consider the case as an individual and/or representative action as well as a derivative action.

on account of laches (25a). This presented the point of laches for appellate review. The law is clear that failure to apply for a temporary injunction does not prevent a restoration of the *status quo* if defendant proceeds *pendente lite* and plaintiff prevails on the merits. *Wingert* v. *First National Bank of Hagerstown,* 223 U. S. 670, 672; *Jones* v. *Securities and Exchange Commission,* 298 U. S. 1, 16-18. The Court of Appeals had recently reaffirmed this rule in *Subin* v. *Goldsmith,* 224 F. 2d, at pp. 761, 762. Hence failure to seek a temporary injunction could not possibly constitute laches. However, instead of ruling on this point, the Court of Appeals evaded it by saying that plaintiff had not attached the proper label to his complaint, but held, in effect, that they would let him attach a new label, come back, and try again. This did not merely delay the review—it predetermined the ruling against plaintiff; for an action of the limited type envisaged by the District Court would certainly be barred by laches if presented in the form of a new complaint brought more than a year after the sale had been approved and consummated. Thus, in effect, the Court of Appeals told plaintiff that they would not rule then on the point of laches—when the authorities were clearly in plaintiff's favor—but they would rule on the point later if and when plaintiff presented it under circumstances where he was sure to lose.

A possible reason for this unusual procedure may be found in the reference by the Court of Appeals to the legally irrelevant fact that plaintiff had not stated in his complaint how many shares of stock he owned (*infra,* p. 22). Compare also the doubt expressed by the majority in *Subin* v. *Goldsmith,* speak-

ing through Medina, J., 224 F. 2d 753, at p. 774, as to federal jurisdiction of a complaint for violation of the proxy statute unless the transaction effected thereby was otherwise illegal or improper, with the holding in this case, per Medina, J., that the federally asserted claim was a mere excrescence because the transaction effected thereby was otherwise illegal and improper (*infra*, p. 27).

This Court is well aware of both the necessity for, and the opportunity for abuse of, stockholder actions. *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541, 547, 548. As long as such actions exist, we submit that points raised therein are entitled to the same character of appellate review as if they were raised in other actions.

We submit that the action of the Court of Appeals in denying such review constitutes such a departure from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision.

III

The holding of the Court below, on the merits, that a corporation may not enjoin or set aside a transaction effected by the violation of a federal statute is in probable conflict with decisions of this Court. The precise question decided presents an important question of federal law which has not been but which should be decided by this Court.

Reference is made to the cases mentioned in the footnote, *supra*, p. 11. See also *Turnstall* v. *Brotherhood of Locomotive Firemen, etc.*, 323 U. S. 210, and the authorities discussed by Mr. Justice Frankfurter in *Montana-Dakota Utilities Co.* v. *Northwestern Public Service Co.*, 341 U. S., at pp. 261, 262. Particularly apposite is *Deckert* v. *Independence Shares Corp.*, 311 U. S. 282, 288, which relates to the field of securities regulation.

Prayer

For the foregoing reasons, petitioner prays that this petition be granted to the end that this case may be reviewed and determined by this Court; that the judgment of the Court of Appeals be reviewed; and that the petitioner be granted such other and further relief as may be proper.

Respectfully submitted,

NORMAN HOWARD
By LEWIS M. DABNEY, JR.
Counsel for the above Petitioner
165 Broadway
New York 6, New York

APPENDIX

Opinion United States Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 43—October Term, 1956.

(Argued October 5, 1956 Decided November 13, 1956.)

Docket No. 24131

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,
Plaintiff-Appellant,

—against—

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,
Defendants-Appellees.

Before:

HAND, MEDINA and HINCKS,
Circuit Judges.

Appeal from a judgment of the United States District Court for the Southern District of New York. Lawrence E. Walsh, *Judge.*

Plaintiff appeals from a judgment entered on an order granting a motion by defendants to dismiss the

complaint for lack of jurisdiction over subject matter, in a stockholder's derivative action against officers and directors of a corporation for alleged waste. Opinion below reported in 140 F. Supp. 507. Affirmed.

LEWIS M. DABNEY, JR., New York City, *for plaintiff-appellant.*

HAYS, PODELL, ALGASE, CRUM & FEUER, New York City (Mortimer Hays, Benjamin Algase, Mortimer Feuer and Martin Mensch, New York City, of Counsel), *for defendants-appellees Sol Furst, Max B. Cohn, Isadore J. Furst, Sol Cohn, Richard C. Noel, Mortimer Hays and Circle Wire & Cable Corp.*

MILBANK, TWEED, HOPE & HADLEY, New York City (A. Donald MacKinnon, New York City, of Counsel), *for defendant-appellee F. Dewey Everett.*

ALEXANDER & GREEN, New York City (Donald M. Dunn, William R. McDermott and J. Kenneth Campbell, New York City, of Counsel), *for defendant-appellee Cerro de Pasco Corporation.*

MEDINA, *Circuit Judge:*

Plaintiff, suing "on behalf of himself and other stockholders of Circle Wire & Cable Corporation," in a derivative action for the benefit of Circle, appeals from a judgment dismissing his complaint for lack of jurisdiction over subject matter.

Diversity of citizenship is not alleged or claimed. The jurisdiction to entertain and determine the action

is said to derive from Section 27 of the Securities Exchange Act of 1934, as amended, 15 U. S. C. section 78aa.[1]

The pivotal factor, about which the allegations of the complaint revolve, is a contract of October 27, 1955, by the terms of which Circle agreed to sell and Cerro de Pasco Corporation agreed to buy all the assets, property and business of Circle for $20,250,000 and the assumption of certain of Circle's liabilities and obligations. Under the applicable New York law, Stock Corporation Law, Section 20, the sale required the consent of two-thirds of Circle's shareholders. A meeting for this purpose was scheduled for November 28, 1955, and on November 3, 1955, a notice of such meeting, and a proxy statement soliciting the votes of the stockholders in favor of the proposed sale, was mailed. This action was commenced

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[1] §78aa. Jurisdiction of offenses and suits

The district courts of the United States, the United States District Court for the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder, or to enjoin any violation of such chapter or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 225 and 347 of Title 28. No costs shall be assessed for or against the Commission in any proceeding under this chapter brought by or against it in the Supreme Court or such other courts.

on November 23, 1955; but no application was made for preliminary injunctive relief, and the sale was affirmed and consummated in due course.

At the time of the sale there were 750,000 shares of Circle stock outstanding, 200,000 of which were sold to the public in 1951. The holdings of the officers and directors of Circle, who, with Cerro, are sued as defendants in this action, amounted to 60.68% of the total outstanding shares. The number of shares owned by plaintiff is not stated; it is merely alleged that at and prior to the sale and at the time of the commencement of the action, he was a stockholder of Circle.

The substance of plaintiff's claim on behalf of Circle is that the individual defendants "to advance their private interests" negotiated the sale for substantially less than the assets of Circle were reasonably worth, and that "such sale will constitute a waste of Circle's assets." It is alleged that the votes of the individual defendants, both as directors and as stockholders are "void and voidable," by reason "of their abuse of their fiduciary position as directors and as controlling stockholders." There are allegations that the suit is not collusive and that no demand had been made upon the defendant directors to refuse to proceed with the sale, or to correct the misstatements and omissions in the proxy statement, hereinafter referred to, or "to bring an action to cancel said contract, or otherwise abandon their plans," as such demand would be futile.

The proxy statement is alleged to be false and misleading in that it understated the cost and present value of Circle's inventory and of its earnings, and by failing to disclose the private interests of the in-

dividual defendants, which are alleged in the complaint.

Section 14(a) of the Securities Exchange Act of 1934 [15 U. S. C. Section 78n(a)] provides:

> "It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national securities exchange or otherwise to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered on any national securities exchange in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule X-14A-9 (17 Code Fed. Reg. §240.14a-9), promulgated pursuant to Section 14(a), reads:

> "No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting, or other communication, written or oral, containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading."

The prayer for relief in the complaint is that proxies given by stockholders of Circle be declared void, that certain of the individual defendants be enjoined from voting as stockholders either in person or by proxy in favor of the sale, that the contract be declared void, and, if consummated *pendente lite,* be rescinded, and that, if restoration of the status quo be impossible, "Circle recover its damages from Cerro and from the individual defendants." In other words, appellant asserted a claim for an injunction against the sale, which, now that the sale has gone through, has become a claim for rescission or for the damages suffered by Circle, not by appellant.

As the case is said to be one "arising under" the laws of the United States, our first inquiry is addressed to appellant's contention that the statutory provisions above quoted create or give rise to a substantive civil right on behalf of Circle, which may be enforced in a derivative action by an individual stockholder. We reject this contention as unsound. We find nothing in the language of Section 14(a) or in the legislative history of the Securities Exchange Act of 1934 to warrant an inference that it was the intention of the Congress to create any rights whatever in a corporation whose stockholders may be solicited by proxy statements prepared in contravention of the statutory mandate.

Ambiguous or equivocal language would hardly be sufficient to support an innovation of such far reaching effects. *Lauritzen* v. *Larsen,* 345 U. S. 571. Here the statute authorizes the formulation of rules and regulations "in the public interest or for the protection of investors." There is literally nothing to sup-

port the view that any substantive rights were created for the benefit of the corporation.

The Securities Exchange Act of 1934 is a comprehensive piece of legislation of wide scope. Significantly, where it was intended to create a right of action in favor of the issuer corporation, the statute makes express provision therefor, as in the case of Section 16(b) [15 U. S. C. Section 78p(b)], relative to short-swing profits. And see *Birnbaum* v. *Newport Steel Corp.,* 2 Cir., 193 F. 2d 461, cert. denied, 343 U. S. 956.

Much is said in the briefs of the respective parties on the subject of the rights of individual stockholders. But no such question is before us here. The complaint is unequivocally cast in terms of the rights of the corporation. And we find no basis for a construction of the complaint as purporting to assert individual rights of plaintiff, either alone, or as suggested by appellant, as the representative of a class. This is not a class suit, nor are any of the characteristic features of a class suit to be found in the complaint.

In *Subin* v. *Goldsmith,* 2 Cir., 224 F. 2d 753, cert. denied, 350 U. S. 883, we left open the question of whether and to what extent Section 14(a) may be construed as creating substantive rights in an individual stockholder. And we leave that question open now.

Appellant has cited certain decisions in cases said to be analogous, which we do not find persuasive, and we think it unnecessary to discuss them.

We turn to the subject of jurisdiction over subject matter. For, if appellant's claim is presented in a case "arising under" the laws of the United States,

a dismissal for lack of jurisdiction is not warranted solely because the interpretation of the federal statute relied upon turns out to be wrong. Accordingly, we shall now examine the allegations of the complaint in order to determine whether, as found by the court below, appellant's claim is for violation of state-created rights, in no real or substantial sense dependent upon the provisions of the Securities Exchange Act of 1934 relative to proxy statements.

The controlling authority is *Gully* v. *First National Bank in Meridian,* 299 U. S. 109, where Mr. Justice Cardozo restates what had long been settled law, to the effect that the federal right relied upon must be an essential element of plaintiff's claim, that it must be of such a character that it will be supported if the federal law is given one construction or effect, and defeated if it receives another. He adds (p. 118):

> "As in problems of causation, so here in the search for the underlying law. If we follow the ascent far enough, countless claims of right can be discovered to have their source or their operative limits in the provisions of a federal statute or in the Constitution itself with its circumambient restrictions upon legislative power. To set bounds to the pursuit, the courts have formulated the distinction between controversies that are basic and those that are collateral, between disputes that are necessary and those that are merely possible. We shall be lost in a maze if we put that compass by."

Applying this test it is clear to us that every essential element of appellant's case depends upon the

common law and the statutes of the State of New York. If the individual defendants who controlled 60.68% of Circle's outstanding stock, in violation of their fiduciary duties as directors and officers of Circle, brought about a sale of Circle's assets for a grossly inadequate sum, all in furtherance of their personal and private interests, the case would be ripe for judgment for rescission of the sale or for damages, wholly irrespective of whether some or all of the individual defendants had participated in the formulation and sending out of a false of misleading proxy statement. The allegations with reference to the proxy statement constitute a mere excrescence or superfluity, tacked onto what are otherwise sufficient allegations of a claim for relief under New York law.

The controversy as to the interpretation to be given Section 14(a) is, therefore, not basic but collateral to appellant's case.

Appellant's further claim of pendent jurisdiction based upon copyright and trademark cases with unfair competition features, such as *Hurn* v. *Oursler,* 289 U. S. 238, and upon other cases, has little to commend it. The doctrine of pendent jurisdiction is only applicable when the federal court has jurisdiction of a substantial claim to begin with; and the policy is that of avoiding piecemeal litigation. See "Note on Pendent Jurisdiction," Hart & Wechsler, The Federal Courts and the Federal System, pp. 802-9. No such rule of policy has any applicability to the present case.

Affirmed.

Judgment

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 13th day of November one thousand nine hundred and fifty-six.

Present: HON. LEARNED HAND,
HON. HAROLD R. MEDINA,
HON. CARROLL C. HINCKS,

Circuit Judges.

NORMAN HOWARD, on behalf of himself & other stockholders of Circle Wire & Cable Corp.

Plaintiff-Appellant

v.

SOL FURST, M. B. COHN, I. J. FURST, S. COHN, R. C. NOEL, M. HAYS, F. D. EVERETT, CERRO DEPASCO CORP & CIRCLE WIRE & CABLE CORP.

Defendant-Appellee

Appeal from the United States District Court for the Southern District of New York

This cause came on to be heard on the transcript of record from the United States District Court for

the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed.

A. DANIEL FUSARO
Clerk

Petition for Rehearing

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 43—October Term, 1956

NORMAN HOWARD, on behalf of himself and other Stockholders of Circle Wire & Cable Corporation,
Plaintiff-Appellant,

—against—

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION and CIRCLE WIRE & CABLE CORPORATION,
Defendants-Appellees.

PETITION FOR REHEARING

To the Honorable Judges of the United States Court of Appeals for the Second Circuit.

On pages 90-91 of its opinion herein this Court has said:

> "Much is said in the briefs of the respective parties on the subject of the rights of individual stockholders. But no such question is before us here. The complaint is unequivocally cast in terms of the rights of the corporation. And we find no basis for a construction of the complaint as purporting to assert individual rights of plain-

tiff, either alone, or as suggested by appellant, as the representative of a class. This is not a class suit, nor are any of the characteristic features of a class suit to be found in the complaint.

"In *Subin* v. *Goldsmith,* 2 Cir., 224 F. 2d 753, cert. denied, 350 U. S. 883, we left open the question of whether and to what extent Section 14(a) may be construed as creating substantive rights in an individual stockholder. And we leave that question open now."

We respectfully submit that the complaint herein does set forth an individual and representative action as well as a derivative action; hence the question left open in *Subin* v. *Goldsmith, supra,* should now be decided.

I.

It is true that plaintiff cast his complaint in the usual form of a stockholder's derivative action. However, Federal pleadings are tested by the facts pleaded, not the theory of the pleader.

Rule 8(a)(2) F. R. C. P. requires that the complaint contain only "a short and clear statement of the claim showing that the pleader is entitled to relief." This means *any* relief, including without limitation the relief to which plaintiff thought he was entitled. This is so even though the Court has to pick a few relevant allegations out of a rambling, inartistic complaint. *Dioguardi* v. *Durning,* 2 Cir., 139 F. 2d 774, 775. The effect and purpose of the Rule was to do away with "theory of the case" pleading,

2 Moore Fed. Prac. 1656-7; and it becomes the Court's duty to "grant the relief to which prevailing party is entitled whether demanded or not." *Gins* v. *Mauser Plumbing Supply Co.*, 2 Cir., 148 F. 2d 974, 976. And the complaint should not be dismissed for insufficiency "unless it appears a certainty that plaintiff is entitled to no relief under any set of facts which could be proved in support of the claim." 2 Moore Fed. Prac. 2245. Hence, without amendment this Court should consider the case as an individual and/or representative* action as well as a derivative action.

II.

Even if the rule were otherwise and "theory of the case" pleading prevailed in the federal court, leave to amend may always be granted. The District Court, construing plaintiff's argument as a request for leave to amend said (25a):

> "Plaintiff has asked leave to amend to allege the claim as a representative action on behalf of all stockholders similarly situated. Although this court would have jurisdiction of such a claim, this application must be denied because the present allegations of the complaint no longer state a claim for which relief may be granted to an individual stockholder."

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* As the Court noted (p. 86) plaintiff herein sued "on behalf of himself and other stockholders of Circle Wire and Cable Corporation." These words are apt in the case of a representative as well as a derivative action.

The District Court then went on to explain that leave to amend was denied only because plaintiff was guilty of laches in failing to apply for a temporary injunction. In other words, the Court denied leave to amend not as a matter of discretion but for legal reasons which plaintiff believes to be erroneous and which he has sought to have reviewed by this Court. Plaintiff believes that he is entitled to such review.

III.

Proper judicial administration requires, we submit, that the points presented be ruled on at this time.

If this Court says nothing further, plaintiff will be in this position: The Court having said that the complaint herein does not present an individual or presentative claim, plaintiff will be free to file a new complaint setting up such claims.* Defendants will then be free to argue (1) that §14(a) of the Securities Exchange Act of 1934 creates no individual or presentative action, and (2) that if it does such claim is barred by laches in failing to apply for a temporary injunction. The most likely result of such defenses is that the District Judge would follow Judge Walsh's previous decision that §14(a) sustained an individual and a representative cause of action of which the Court had jurisdiction, but that such action was barred by laches. Whatever the decision, there

* It seems clear that the present decision of this Court would not be *res judicata* as to such action; and neither would Judge Walsh's decision, since it was affirmed on different grounds. However, if there is any doubt as to this point there is all the more reason why plaintiff should now have his day in court as to the validity of an individual or representative action.

would have to be another appeal to settle the law. Judicial economy of effort would seem to forbid such useless procedure.

IV.

Our reasons for considering that the lower Court erred in deciding that plaintiff's individual and representative actions were barred by laches are set forth in our Main Brief, pp. 22-24. They are, in brief, that a defendant who proceeds *pendente lite* in the face of a prayer for injunction, proceeds at his peril, and, if plaintiff finally prevails, must restore the *status quo*. *Wingart* v. *National Bank of Hagerstown,* 223 U. S. 670, 672; *Jones* v. *Securities and Exchange Commission,* 298 U. S. 1, 16-18; *Subin* v. *Goldsmith,* 2 Cir., 224 F. 2d 753, 761, 762. Hence failure to apply for a temporary injunction cannot possibly be laches. Defendants have not attempted to answer this argument.

Accordingly, plaintiff-appellant prays for a rehearing; that on such rehearing the judgment be reversed and the cause remanded to the District Court with instructions to try the cause as an individual and representative action; or, in the alternative, that leave to amend be granted to allege such an action.

Respectfully submitted,

LEWIS M. DABNEY, JR.
Attorney for Plaintiff-Appellant
165 Broadway
New York City

Decision on Rehearing

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

NORMAN HOWARD, on behalf of himself and other Stockholders of Circle Wire & Cable Corporation,
Plaintiff-Appellant

—against—

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION and CIRCLE WIRE & CABLE CORPORATION,
Defendants-Appellees

Before HAND, MEDINA and HINCKS, *Circuit Judges*

On Petition for Rehearing

LEWIS M. DABNEY, JR., New York City
for plaintiff-appellant

PER CURIAM

Petition for rehearing denied.

s/ LEARNED HAND
Learned Hand

s/ HAROLD R. MEDINA
Harold R. Medina

s/ CARROLL C. HINCKS
Carroll C. Hincks

C. J. J.

dated; December 10, 1956

Order on Rehearing

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the tenth day of December, one thousand nine hundred and fifty-six

Present: HON. LEARNED HAND,
HON. HAROLD R. MEDINA,
HON. CARROLL C. HINCKS,
Circuit Judges.

NORMAN HOWARD, on behalf of himself and other stockholders of Circle Wire & Cable Corporation
Plaintiff-Appellant

v.

SOL FURST et al.
Defendants-Appellees

A petition for a rehearing having been filed herein by counsel for the appellant

Upon consideration thereof, it is

Ordered that said petition be and hereby is denied.

A. DANIEL FUSARO
Clerk

APR 5 1957
JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 828

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,

Petitioner,

against

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,

Respondents.

BRIEF IN OPPOSITION ON BEHALF OF RESPONDENTS SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, AND CIRCLE WIRE & CABLE CORPORATION (NOW C.W.C. LIQUIDATING CORP.)

MORTIMER HAYS,
Counsel for Respondents Sol Furst, Max B. Cohn, Isadore J. Furst, Sol Cohn, Richard C. Noel, Mortimer Hays and Circle Wire & Cable Corp. (now C.W.C. Liquidating Corp.).

BENJAMIN ALGASE,
MORTIMER FEUER,
MARTIN MENSCH,
Of Counsel.

A. DONALD MACKINNON,
Counsel for Respondent F. Dewey Everett.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 828

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,

Petitioner,

against

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,

Respondents.

BRIEF IN OPPOSITION ON BEHALF OF RESPONDENTS SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT AND CIRCLE WIRE & CABLE CORPORATION*

Petitioner seeks a writ of certiorari to review an order of the Court of Appeals for the Second Circuit which affirmed a judgment of the United States District Court for the Southern District of New York dismissing petitioner's complaint (1) for want of federal jurisdiction, and (2) for failure to state a claim upon which relief might be granted. There is no diversity of citizenship.

* This corporation is in the process of liquidation. Its name has been changed and is now C.W.C. Liquidating Corp.

It is the respectful submission of respondents that the court below applied well-settled law to the complaint here, that no reasons have been advanced by petitioner for review by this Court, and that, therefore, the petition should be denied.

Questions Presented for Review

Respondents cannot agree that the statement in the petition of "Questions Presented for Review" (pp. 2-3) accurately reflects the questions presented. Respondents deem it necessary to restate them as follows:

(1) Whether the Court of Appeals correctly held that a stockholders' derivative suit was dependent on New York Law and did not arise under the laws of the United States where the suit sought rescission of a sale of corporate assets and charged that the sale was wasteful, disadvantageous to the corporation, and motivated by self-interest on the part of certain directors, and that the approval of stockholders to the sale required by Section 20 of the New York Stock Corporation Law was obtained by means of an allegedly false proxy statement in violation of Section 14(a) of the Securities Exchange Act of 1934 and Rule X-14A-9 promulgated thereunder.

(2) Whether the Court of Appeals correctly held that Section 14(a) of the Securities Exchange Act of 1934 and Rule X-14A-9 promulgated thereunder did not create substantive corporate rights enforceable by a stockholder in a derivative action.

Statutes Involved

To the "statutes involved", recited at pages 3-4 of the petition, there should be added Section 20 of the Stock Corporation Law of the State of New York, McKinney

Consol. Laws, c. 59, which is referred to in the complaint (par. 9, pp. 6a-7a).*

That section reads in material part as follows:

> "A stock corporation, except as otherwise provided by law or by its certificate of incorporation or other certificate filed pursuant to law, may voluntarily sell, lease or exchange its property, rights, privileges and franchises, or any interest therein or any part thereof; provided, however, that if such sale, lease or exchange is not made in the regular course of business of the corporation and involves all or substantially all of its property, rights, privileges and franchises, or an integral part thereof essential to the conduct of the business of the corporation, such sale, lease or exchange shall not be made without the consent of either the holders of record of all of its outstanding shares entitled to vote thereon given in writing without a meeting or the holders of record of two-thirds of its outstanding shares entitled to vote thereon obtained at a meeting of the stockholders called pursuant to section forty-five. Franchises within the state may be sold only to a domestic corporation. * * *"

Statement of the Case

1. The Complaint

The complaint purports to allege a derivative stockholders' action on behalf of Circle Wire & Cable Corporation ("Circle" hereafter), a corporation organized under the laws of the State of New York, against Cerro de Pasco Corporation ("Cerro" hereafter), also a corporation organized under the laws of the State of New York (Complaint, par. 1, pp. 3a-4a), and the directors of Circle.

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* Paragraph references hereafter are to paragraphs of the complaint. Page references, "a", are to the appendix to petitioner's brief in the Court of Appeals.

After making certain formal allegations, the complaint alleged that Circle was dominated by two of the individual defendants (pars. 4-7, pp. 4a-6a), who owned or controlled over 60 per cent of Circle's outstanding stock (par. 6, pp. 5a-6a) and that Circle and Cerro entered into a contract whereby Cerro agreed to purchase all of Circle's assets except good will (par. 9, pp. 6a-7a). It was further alleged in paragraph 9 that, by virtue of Section 20 of the New York Stock Corporation Law, such sale required the approval of the holders of at least two-thirds of Circle's outstanding stock, and such approval was made an express condition of the carrying out of the agreement of sale. It was alleged that the approval of stockholders made necessary by New York Law was solicited by means of a proxy statement which (on the information and belief of the pleader) was false and misleading. The proxy statement was alleged to have understated both inventory (by over eight million dollars) and earnings for the years 1952-1954 and the first nine months of 1955, and failed to disclose that certain directors had a personal motive for the sale, *i.e.*, that the continuance of Circle in business would have increased the risk of discovery of such understatements, and that the sale of Circle's assets was motivated by a desire on the part of the controlling stockholders and directors to reduce or eliminate such risk (pars. 14-16, pp. 9a-11a).

The complaint then alleged further that:

> "the proposed sale is disadvantageous to Circle in that the fair value of Circle's assets and business is substantially in excess of the net price to be received in such sale. * * * If consummated, such sale will constitute a waste of Circle's assets" (Par. 18, pp. 11a-12a).

The complaint asserted, finally, that it would be

> "more advantageous to Circle and its public stockholders to continue to carry on its business than

> to sell to Cerro on the terms proposed, as would be readily apparent if the accounts of Circle were correctly stated" (Par. 19, p. 12a).

and

> "The votes of the defendant directors to approve the sale are void and voidable on account of their materially adverse interests to the stockholders. The votes of Messrs. Furst and Cohn [allegedly controlling stockholders], as stockholders, if cast in favor of the sale, will be void or voidable on account of their abuse of their fiduciary position as directors and controlling stockholders" (Par. 20, p. 12a).

Relief was requested substantially as follows: (a) that all proxies given by Circle's stockholders be declared void and their voting be enjoined; (b) that certain of the stockholders be enjoined from voting at all in favor of the sale; and (c) that the contract between Circle and Cerro be voided, or if the sale be consummated *pendente lite,* it be rescinded; and that, if restoration of the status quo be impossible, Circle recover damages from Cerro and the individual defendants (p. 13a).

2. Proceedings Below

Petitioner did not move below for temporary relief. The stockholders' meeting was held as scheduled and approximately 97 per cent of the shares voting approved the sale (the shares voting at the meeting constituting more than 89 per cent of the total number outstanding). Pursuant to the agreement between the parties and the approval of Circle's stockholders, the purchase of Circle's assets by Cerro was consummated. An affidavit containing these facts was received by the District Court pursuant to Federal Rule of Civil Procedure 12(b) (28 U.S.C.).

Wholly apart from the consummation of the sale, defendants moved to dismiss the complaint (a) for want of

jurisdiction on the ground that the action did not arise under the Securities Exchange Act of 1934, because violation of that Act was not an essential element of plaintiff's claim but was, at best, merely involved incidentally or collaterally; and (b) for failure to state a claim upon which relief might be granted on the ground that, whether or not a private civil action were available under Section 14(a) of the Securities Exchange Act, the corporation was not in the class protected by said Section and hence a derivative action would not lie.

The District Court dismissed the complaint (140 F. Supp. 507 [S.D. N.Y., 1956]). It determined that a private right of action for violation of Section 14(a) was not given to the corporation but was accorded to the stockholders, individually. Accordingly, since the complaint alleged a derivative cause, it failed to set forth a claim upon which relief might be granted. The District Court also dismissed for lack of jurisdiction, relying, *inter alia*, on *Gully* v. *First National Bank in Meridian*, 299 U. S. 109 (1936).

The Court of Appeals affirmed. It was of the opinion that Section 14(a) of the Securities Exchange Act did not give rise to a substantive civil right on behalf of a corporation which might be enforced derivatively by an individual stockholder. Hence it held that the complaint failed to state a claim upon which relief might be granted. It specifically left open the question of whether and to what extent Section 14(a) created substantive rights in an individual stockholder, since that question was not before it. The Court of Appeals also found no basis upon which the federal courts might assume jurisdiction (238 F. 2d 790 [2nd Cir. 1956]).

ARGUMENT FOR DENYING THE WRIT

I

There is no basis here for any claim of conflict. The Court of Appeals, in finding lack of jurisdiction, followed and applied *Gully* v. *First National Bank*, 299 U. S. 109 (1936), and accorded full recognition to the principles of *Bell* v. *Hood*, 327 U. S. 678 (1946).

1. Petitioner claims a "probable" conflict between the decision of the Court of Appeals and applicable decisions of this Court (Petition, pp. 9, 17). Respondents note preliminarily that a claim of "probable" conflict is not sufficient, under this Court's present rules, to justify the grant of certiorari (Rule 19(1)(b); *cf.* former Rule 38(5)(b)).

2. Petitioner misconceives the basis for the dismissal of his complaint for want of jurisdiction. It was dismissed not because petitioner pleaded a "wrong" actionable under both state and federal law (Petition, p. 12), but because the "wrong" was not dependent upon federal law at all. *Bell* v. *Hood*, 327 U. S. 678 (1946), upon which petitioner relies, is relevant only if petitioner has pleaded a claim which meets the criteria for the existence of federal jurisdiction in the first instance. Two courts below, applying the principles for the determination of the existence of federal question jurisdiction contained in the leading case of *Gully* v. *First National Bank in Meridian*, 299 U. S. 109 (1936), have held that this complaint does not so plead.

In that case, Mr. Justice Cardozo summarized some of the "well established" tests for determining "how and

when a case arises under the Constitution or laws of the United States":

> "To bring a case within the statute, a right or immunity created by the Constitution or laws of the United States must be an element, *and an essential one,* of the plaintiff's cause of action [citing cases]. The right or immunity must be such that it will be supported if the Constitution or laws of the United States are given one construction or effect, and defeated if they receive another [citing cases]" (299 U. S. at pp. 112-13; emphasis supplied).
>
> • • • • •
>
> "A suit to enforce a right which takes its origin in the laws of the United States is not necessarily, or for that reason alone, one arising under those laws, for a suit does not so arise unless it really and substantially involves a dispute or controversy respecting the validity, construction or effect of such a law, upon the determination of which the result depends" (p. 114).

And he added:

> "Not every question of Federal law emerging in a suit is proof that a federal law is the basis of the suit" (p. 115).

Mr. Justice Cardozo stated finally:

> "As in problems of causation, so here in the search for the underlying law. If we follow the ascent far enough, countless claims of right can be discovered to have their source or their operative limits in the provisions of a federal statute or in the Constitution itself with its circumambient restrictions upon legislative power. To set bounds to the pursuit, the courts have formulated the distinction between controversies that are basic and

those that are collateral, between disputes that are necessary and those that are merely possible. We shall be lost in a maze if we put that compass by" (p. 118).

See also *Skelly Oil* v. *Phillips Petroleum,* 339 U. S. 667, 671-4 (1949).

The existence of a federal question is determined from the facts pleaded in the complaint. Unless the complaint states facts which establish that the federal statute is an essential element of plaintiff's cause, jurisdiction will not lie. *Louisville & Nashville R. Co.* v. *Mottley,* 211 U. S. 149 (1908); *Tennessee* v. *Union & Planters Bank,* 152 U. S. 454 (1894); *Little York Gold Washing & Water Co.* v. *Keyes,* 96 U. S. 199 (1878).

Examination of the complaint here makes patent that the instant action is one which is founded on state common and statutory law.

This is a stockholders' derivative suit claiming breach of fiduciary duty, the essential elements of which are allegations of common law waste and non-compliance with New York statutory law. The claim of breach of fiduciary duty resulting in common law waste and the claims of violation of Section 20 of the New York Stock Corporation Law are provable, if true, without reference to the federal statute or rule. The suit, regardless of whether the proxy material was improper, seeks to upset the contract of sale, which was entered into before any purported violation of Section 14(a) took place, as being wasteful and the result of self-interest. Waste and self-dealing are not claims under the federal statute, and since consents required by Section 20 of the New York Stock Corporation Law, allegedly obtained by fraud in proxy statements, would be invalid at common law, the federal statute adds nothing to plaintiff's allegations asserting an actionable

wrong. The questions of fact and law would be the same even though the federal statute had never been enacted.*

The thrust of plaintiff's claim is toward the rescission of the sale of assets by Circle to Cerro (or, in the alternative, damages). Even if that claim were not based upon allegations of breach of fiduciary duty and of waste of corporate assets, it would necessarily be based upon New York law, *i.e.*, Section 20 of the New York Stock Corporation Law, which sets forth the conditions under which a corporation may sell its assets. Proxies approving the sale were solicited from stockholders because of the requirements contained in Section 20, not because of the requirements of the federal statute. The federal statute and rule do not contain the conditions under which a New York corporation may sell its assets, or the conditions under which the sale may be nullified. If the transaction is to be voided, it is because the consents received did not comply with the requirements of Section 20, not because a federal statute was violated.

The Securities Exchange Act, therefore, is not an essential element of plaintiff's claim, and the result does not depend upon the construction or effect to be given to

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* In *Montana-Dakota Utilities Co.* v. *Northwestern P. S. C.*, 341 U. S. 246 (1950), upon which petitioner relies, Mr. Justice Jackson stated as follows:

> "If the petitioner's grievance arises from active fraud and deceit, it gains nothing from the Federal Act. Such an action would have been maintainable if no Federal Power Act had been enacted. Before the Act, petitioner would have had no statutory right to a reasonable rate, but it did have a common-law right not to be defrauded into paying an excessive or unreasonable one. The Federal Act adds nothing to fraud as an actionable wrong, and, therefore, to find a cause of action of this character would only be to dismiss it for want of diversity" (p. 252).

that statute. The Securities Exchange Act is only collaterally or incidentally, if at all, involved.*

This is not a case in which the claim asserted arises both under common (or state) and federal law. *Bell* v. *Hood, supra,* held that where the facts gave rise to a claim both under the common and federal law, federal jurisdiction was nevertheless present. But in *Bell,* the criteria for federal jurisdiction contained in *Gully* were satisfied since plaintiff there sought recovery "squarely on the ground" that defendants violated the Constitution (327 U. S. 678, 681). Accordingly, Mr. Justice Black pointed out that the violations of the Constitution alleged there formed "the sole basis of the relief sought" (327 U. S. 683). The cases cited by petitioner (Petition, p. 12), viz., *Fitzgerald* v. *Pan-American World Airways,* 229 F. 2d 499 (2d Cir., 1956), and *Fielding* v. *Allen,* 181 F. 2d 163 (2d Cir., 1950), were applications of the doctrine of *Bell* v. *Hood.* No more than *Bell* do these cases touch the decision of the Court of Appeals here.**

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* To the same effect is *Lapchak* v. *Sisto* (not officially reported), C.C.H. Fed. Sec. L. Rep. §90, 721 (S.D.N.Y., 1955), which similarly purported to involve Section 14(a) of the Securities Exchange Act and was similarly dismissed for lack of federal jurisdiction. See also *Nelson* v. *Leighton,* 82 F. Supp. 661 (N.D. N.Y., 1949); *Crawford* v. *Pituch,* 91 F. Supp. 626 (W. D. Pa., 1950).

** Also irrelevant are the other cases cited by petitioner purportedly in support of his jurisdictional proposition:

(1) *Hurn* v. *Oursler,* 289 U. S. 238 (1933) (Petition, p. 11), does not apply unless the court has jurisdiction of a sufficient federal claim in the first instance, which the Court did not have here. That case is not applicable where the federal claim is dismissed on its face and before trial. *Mass. Univ. Conv.* v. *Hildreth & Rogers Co.,* 87 F. Supp. 822 (D. Mass., 1949), affirmed on opinion below, 183 F. 2d 497 (1st Cir., 1950); *State of Georgia* v. *Wenger,* 94 F. Supp. 976 (E. D. Ill., 1950), affirmed 187 F. 2d 285 (7th Cir., 1951). See also "Note on Pendent Jurisdiction," Hart & Wechsler, The Federal Courts and The Federal System (1953), pp. 802-9. And finally, *Hurn* does not apply to this case because the facts in respect of the alleged "federal" claim

II

The Court of Appeals properly held that Section 14(a) of the Securities Exchange Act did not create any rights in a corporation.

The complaint concededly asserts a derivative cause on behalf of Circle Wire & Cable Corp.

The complaint itself states:

> "Plaintiff brings this action on behalf of Circle against Cerro and the remaining defendants" (par. 3, p. 4a).

In his main brief to the Court of Appeals (pp. 5-6, note), petitioner stated:

> "Plaintiff's position was and is that he has the right to bring a derivative action; and the action is cast in such form."

(fraud in the proxy statement) are not substantially identical with the facts involved in the common law claim (breach of fiduciary duty and waste of corporate assets).

(2) In *Montana-Dakota Utilities Company* v. *Northwestern P. S. C.*, 341 U. S. 246 (1950) (Petition, p. 11), the complaint charged that an interlocking directorship between utilities was used to deprive one utility of its federally conferred right to reasonable rates and charges. The complaint accordingly disclosed a controversy which turned squarely on the reasonableness under the Federal Power Act of those rates and charges, and, therefore, federal jurisdiction was present. The Court dismissed on the merits because it held that courts were not equipped to grant the relief requested.

(3) In *Subin* v. *Goldsmith*, 224 F. 2d 753 (2d Cir., 1955), cert. den. 350 U. S. 833 (1955) (Petition, p 11, note), jurisdiction was present because of diversity of citizenship and hence no jurisdictional question was raised. The allegations of the complaint referable to Section 14(a) of the Securities Exchange Act were dismissed as insufficient because fraud had not been alleged with sufficient particularity.

In the other cases cited with *Subin* v. *Goldsmith* in the note on page 11 of the Petition, jurisdiction was not in question because federal law was the basis of the action.

In his application to the Court of Appeals for rehearing, the petitioner added:

> "It is true that plaintiff cast his complaint in the usual form of a stockholder's derivative action. * * *" (Petition, p. 31).

Both the District Court and the Court of Appeals considered the claim to be what petitioner stated it to be, a stockholders' derivative suit, and held that Section 14(a) of the Securities Exchange Act did not create any substantive rights in favor of the corporation.

Preliminary to a discussion of the correctness of this holding, it should be pointed out that, in his brief to the Court of Appeals (pp. 5-6), petitioner argued that "if the complaint, construed as a representative action, states a claim upon which relief may be granted, that is the way it should be construed," and in his application to the Court of Appeals for a rehearing, petitioner urged that the complaint set forth "an individual and representative action as well as a derivative action" (Petition, p. 31).

The Court of Appeals rejected this contention and held that the complaint was unequivocally cast in terms of the rights of the corporation.* The Court of Appeals said:

* Petitioner's criticism of the Court of Appeals because of its purported failure to review a point discussed by the District Court (Petition, pp. 14-16) is unwarranted. The District Court had understood that petitioner had, orally, upon the argument, asked for leave to amend his complaint to allege a representative cause, a request which petitioner denies making (Petitioner's main brief to the Court of Appeals, pp. 5-6). The Court stated that it would deny the application because the sale had taken place and rescission of a completed transaction by a stockholder in his individual or representative capacity was not authorized by Section 14(a) of the Securities Exchange Act. The Court went on to state that the Court has power, upon the complaint of a stockholder, individually or representatively, either to correct a false proxy statement or enjoin the holding of the stockholders' meeting until correction can be made. The Court stated that this relief might have been available had petitioner acted promptly, and added that in the absence of injunctive relief, damages might be recov-

"We find no basis for a construction of the complaint as purporting to assert individual rights of plaintiff, either alone, or as suggested by appellant, as the representative of a class. This is not a class suit, nor are any of the characteristic features of a class suit to be found in the complaint" (238 F. 2d at 793, Petition, p. 25).*

In view of the nature of the claim and facts alleged in the complaint, the Court properly refused to muddy the waters by entertaining a claim that was not before it. In the exercise of its discretion, it properly denied the belated request of petitioner for leave to amend to set forth a new and representative cause, a request made for the first time in the litigation on the petition for rehearing.

Plaintiff argues his cause as though there were no possibility of relief upon the complaint here in question

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ered. It was in the context of the discussion of petitioner's possible alternatives that the reference by the District Court to "laches" must be understood. The Court of Appeals properly refrained from passing on the rights secured to stockholders, individually or representatively, by Section 14(a), since the point was not before it.

* The distinctions between a representative and a derivative action are significant and material. The two different kinds of actions are brought on behalf of different parties, the stockholders in one case, the corporation in the other. They raise different problems relating to the adequacy of representation and standing to raise the question, and the effect of such judgment as is rendered differs depending on the nature of the action (see, generally, 3 Moore's Fed. Prac., 3401 *et seq.*, 3506-11 [2d ed., 1951]). In this context, since the objective of the action is the rescission of the sale by Circle to Cerro, or alternatively, the recovery of damages by Circle, the action is unquestionably derivative. *Continental Insurance Company* v. *N. Y. & H. R. R. Co.*, 103 App. Div. 282, 284-5 (1st Dept., 1903), aff'd 187 N. Y. 225 (1907); Fletcher Cyclopedia, Corporations (1943 Rev. ed.), §5927. The allegations of waste in the complaint must likewise be asserted derivatively. *Green* v. *Victor Talking Machine Co.*, 24 F. 2d 378, 380, 381 (2d Cir., 1928); *Niles* v. *N. Y. C. & H. R. R. Co.*, 176 N. Y. 119, 123 (1903); *Kavanaugh* v. *Commonwealth Trust Company*, 181 N. Y. 121, 123 (1905). The argument made and the cases cited in the note at page 14 of the petition are inapposite. This is not a question of picking out allegations from an "inartistic" complaint, but involves a substantive matter of importance.

except in the Federal Court. But if petitioner insists on a derivative action raising claims of damage to the corporation under common or state law, he may bring his action in a New York State court. The New York State Supreme Court is the proper forum for a derivative action involving common law claims of corporate waste and self-dealing on the part of directors. And it is, also, where a derivative action for violation of Section 20 of the New York Stock Corporation Law will lie (*Bassett* v. *Battle,* 253 App. Div. 893, 1 N. Y. S. 2d 869 [2d Dept., 1938]; *Cachules* v. *116 E. 57th Street* [not officially reported], 125 N. Y. S. 2d 97 [Sup. Ct., N. Y. Co. 1953]).

Alternatively, if petitioner has an individual or representative claim which arises under Section 14(a) of the Securities Exchange Act, he may bring it in the federal court individually, or, upon compliance with the appropriate rules relating to the representation of a class, representatively. The Court of Appeals expressly left open "the question of whether and to what extent Section 14(a) may be construed as creating substantial rights in an individual stockholder" (238 Fed. at 793, Petition p. 25).

Upon consideration of the complaint as asserting a derivative cause, the Court of Appeals affirmed the determination of the District Court dismissing the complaint for failure to state a claim upon which relief could be granted, on the ground that Section 14(a) of the Securities Exchange Act did not create any rights in a corporation. The Court of Appeals found "nothing in the language of Section 14(a) or in the legislative history of the Securities Exchange Act of 1934 to warrant an inference that it was the intention of the Congress to create any rights whatever in a corporation whose stockholders may be solicited by proxy statements prepared in contravention of the statutory mandate." The Court added that:

"The Securities Exchange Act of 1934 is a comprehensive piece of legislation of wide scope. Significantly, where it was intended to create a right of action in favor of the issuer corporation, the statute makes express provision therefor, as in the case of Section 16(b) [15 U.S.C. Section 78p(b)], relative to short-swing profits. And see *Birnbaum* v. *Newport Steel Corp.*, 2 Cir., 193 F. 2d 461, cert. denied, 343 U. S. 956."*

* The legislative history of Section 14(a) of the Securities Exchange Act supports the determination of the Court of Appeals. At one point it was proposed that this section afford protection to the "issuer", *i.e.*, the corporation, as well as to the stockholders. But Congress specifically deleted language which would have so provided, as is shown by the following:

(i) The original Senate-House bills (S. 2693, Feb. 6 [calendar day, Feb. 9], 1934; H. R. 7852 and 7855, Feb. 10, 1934) required proxy statements to be "in such form and detail as the Commission may by rules and regulations prescribe *in the public interest or for the protection of investors.*"

(ii) The next House bill (H. R. 8720, March 19, 1934) was substantially the same as above.

(iii) The revised Senate bill (S. 3420, April 17 [calendar day April 20], 1934) eliminated "in the public interest," and limited coverage to *"the protection of investors."*

(iv) At this point the House incorporated a substantial change in the proposed proxy statute (H. R. 9323, Union Calendar No. 302, April 25, 1934), changing the bill to read: "* * * such rules and regulations as the Commission may prescribe as necessary or appropriate in the interest of the *issuer* of such security or for the protection of investors in the securities of such issuer" (§13(a)).

(v) This latter bill immediately thereafter went into joint Senate-House conference, was amended, and emerged as H. R. 9323 "Corrected Print," *which deleted the reference to the "issuer" and instead applied solely "in the public interest or for the protecton of investors"* (§14(a)). (Emphasis ours throughout.)

The proxy statute as enacted, 48 Stat. 895, provided coverage as the S.E.C. found necessary or appropriate "in the public interest or for the protection of investors" (§14(a)).

In the context of Section 14(a) the term "issuer", of course, refers to an issuer of securities in respect of which a proxy is solicited (Proxy Rule X-14A-1, 17 Code Fed. Reg. 240, 14A-1). (Here, the "issuer" was Circle.)

In so holding, the Court was merely following the well settled rule that those claiming the benefit of statutory rights and remedies must bring themselves precisely within the class sought to be protected (*Birnbaum* v. *Newport Steel Co.*, 193 F. 2d 461 [2nd Cir., 1952], cert. den. 343 U. S. 956 [1952];* *Joseph* v. *Farnsworth Radio & Television Corp.*, 99 F. Supp. 701 [S.D. N.Y., 1951], aff'd on opinion below, 198 F. 2d 883 [2d Cir., 1953]; *Patterson* v. *Sears-Roebuck & Co.*, 196 F. 2d 947, 949 [5th Cir., 1952]).

The cases cited by petitioner (p. 17) are irrelevant to the question decided by the Court of Appeals. Petitioner apparently relies on some language in cases decided by this Court whose holdings are inapposite and are stated below.*

The language relied upon relates to the proposition that a duty declared by Congress is enforceable in the

* The *Birnbaum* case involved Section 10(b) of the Securities Exchange Act which provides coverage, precisely as does Section 14(a) of that Act, "in the public interest or for the protection of investors" (15 U.S.C. §78j(b) 48 Stat. 891). The Court of Appeals affirmed the dismissal of a complaint charging breach of fiduciary duty by corporate insiders, on the ground that the language in Section 10(b) was not "directed at the fraudulent mismanagement of corporate affairs * * *". It added that when Congress intended to protect stockholders of a corporation against breach of fiduciary duty by corporate insiders, it left no doubt as to its meaning, referring to Section 16(b) of the Securities Exchange Act (193 F. 2d at 463-4).

* *Tunstall* v. *Brotherhood of Locomotive Firemen, etc.*, 323 U. S. 210 (1944), held that federal jurisdiction existed over an action which sought injunction and damages for the failure of the union bargaining representative of plaintiff's craft to perform the duty imposed on it by a federal statute. *Montana-Dakota Utilities Co.* v. *Northwestern P. S. C.*, 341 U. S. 246, 261, 262 (1951), involved the distinction, settled by *Bell* v. *Hood, supra*, between jurisdiction and merits (see *supra*, p. 12 fn.). *Deckert* v. *Independent Shares Corporation*, 311 U. S. 282 (1940), while relating to the field of securities regulation, had nothing to do with the instant matter. That case held that in an action properly brought under the Securities Act of 1933, (1) plaintiff was not restricted to a money judgment but could obtain equitable relief, and (2) that in an action brought under said statute, jurisdiction would attach irrespective of the amount in controversy.

courts despite the absence of a formulated sanction. The question raised here was not whether any private relief might be had for a violation of Section 14(a), but whether that section created any rights in a corporation which could be asserted in a derivative suit.

In the other cases cited by petitioner on this point and discussed *supra,* pages 11-12, note (Petition, p. 17, referring to Petition, p. 11, note), either the question did not arise because the case was disposed of otherwise (*Subin* v. *Goldsmith, supra*), or it was held merely that a civil action would lie under the statutes involved in those cases.* They do not touch the question of whether a civil action exists in favor of a corporation under Section 14(a). See the concurring opinion of Judge Lumbard, with which Judge Swan agreed, in *Spirt* v. *Bechtel,* 232 F. 2d 241 (2d Cir., 1956).

* None of those actions was derivative, except that in *Goldstein* v. *Groesbeck,* 142 F. 2d 422 (2d Cir., 1944), which involved a statute whose express purpose was to protect subsidiaries from the overreachings of parent holding company (Public Utility Holding Company Act.) A derivative action was therefore permitted on behalf of the subsidiary against the parent.

CONCLUSION

Wherefore, it is respectfully submitted that the petition for certiorari be denied.

Respectfully submitted,

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FILED
APR 5 1957
JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 828

NORMAN HOWARD, on behalf of himself and other Stockholders of CIRCLE WIRE & CABLE CORPORATION,

Petitioner,

against

SOL FURST, MAX B. COHN, ISADORE J. FURST, SOL COHN, RICHARD C. NOEL, MORTIMER HAYS, F. DEWEY EVERETT, CERRO DE PASCO CORPORATION, and CIRCLE WIRE & CABLE CORPORATION,

Respondents.

BRIEF IN OPPOSITION OF RESPONDENT CERRO de PASCO CORPORATION

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Respondents.

BRIEF IN OPPOSITION OF RESPONDENT CERRO de PASCO CORPORATION

The respondent Cerro de Pasco Corporation ("Cerro") has been brought into this case because the petitioner is seeking to rescind on behalf of Circle Wire & Cable Corp. ("Circle") the sale of the assets of that corporation to Cerro. That claim for rescission[1] is based on Section 20 of the New York Stock Corporation Law and on the New York common law. Although the complaint alleges that Cerro had notice of false and misleading statements in the proxy material sent out by Circle's directors to petitioner and the other Circle stockholders (Appellant's Appendix in the Court of Appeals, p. 12a), it does not allege that Cerro performed any act prohibited by federal law or omitted to do anything required by such law.

[1] Petitioner sought alternative relief by way of damages "only if restoration of the status quo be impossible" (Appellant's Appendix in the Court of Appeals, p. 13a).

Cerro here was in the position of a purchaser of the assets of Circle. It owed no duty to Circle except to perform its contract for the purchase of Circle's assets. There is no allegation that Cerro breached that duty.

Petitioner's claim against Cerro therefore is a claim for rescission arising under state law, separate and distinct from any claim arising out of an alleged violation of the Securities Exchange Act. *Pearce* v. *Pennsylvania R. Co.*, 162 F. 2d 524, 526, 527 (3rd Cir. 1947), cert. denied 332 U. S. 765 (1947).[3]

Accordingly, wholly apart from the question whether the District Court had jurisdiction over the claim against the individual respondents, that Court had no jurisdiction over petitioner's claim against Cerro for rescission.

CONCLUSION.

It is respectfully submitted that the petition for a writ of certiorari be denied.

Dated, April 4, 1957.

Respectfully submitted,

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[3] See also *Hurn* v. *Oursler*, 289 U. S. 238, 245-246 (1933); *United States* v. *Dooley*, 231 F. 2d 423 (9th Cir. 1955); *Wassermon* v. *Perugini*, 173 F. 2d 305, 306 (2nd Cir. 1949).

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Respondents.

REPLY BRIEF ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

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Respondents.

REPLY BRIEF ON PETITION FOR WRIT OF CERTIORARI

I

1. After arguing first that the complaint herein was based wholly on state-law grounds (Br. 4-5)[1] and second that it was based "essentially" on state-law

[1] This argument is supported by the simple device of enumerating all the state-law grounds referred to in the complaint and omitting all reference to the federal grounds including any reference to the federal statute on which plaintiff relies. See Pet. 5-7, Complaint, Pars. 2, 10-15; 4a, 7a-10a.

grounds (Br. 8-9),[2] respondents Furst et al. finally meet the issue and assert, third, (as they must in order to defeat federal jurisdiction, *Bell* v. *Hood, supra*) that "the 'wrong' was not dependent upon federal law at all" (Br. 7), and that "this is not a case in which the claim asserted arises both under common (or state) and federal law." (Br. 11)

Respondents' failure to rely on their first two positions is well advised. The most superficial examination of the complaint rebuts the first; and the second is not the law. If it were law, all the violator of a federal statute would have to do in order to go scot free would be to take care to violate state law at the same time; then he could plead that his illegal act was "really" or "essentially" a violation of state law and defeat federal jurisdiction. We need not labor this point; because the line of cases headed by *Hurn* v. *Oursler,* 289 U. S. 238, specifically covers the situation where the same course of conduct violates both state and federal law. Up to the decision in the instant case such dual violation had been considered a reason for asserting jurisdiction over the state-created wrong, rather than abandoning jurisdic-

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[2] When an action is based on both federal and state-law grounds, "the party who brings a suit is master to decide what law he will rely upon." *Bell* v. *Hood,* 327 U. S. 678, 681.

Respondents' argument, Br. 9, that it was state law which required defendants to solicit proxies, hence fraudulent solicitation, is "essentially" a violation of state law, even though federal law expressly forbids fraudulent solicitation, proves too much. Except in the rare instance of federal incorporation, it is always state law which determines when stockholder consent is necessary, and hence when solicitation of proxies is required. If respondents' argument is valid, Sec. 14 of the Securities Exchange Act of 1934 applies only to federally incorporated companies.

tion over the federally created wrong. Respondents finally concede this when they say (Br. 11), "*Bell* v. *Hood, supra,* held that where the facts give rise to a claim both under the common and federal law, federal jurisdiction was nevertheless present."

The case then comes down to the simple question of whether the complaint charges a violation of federal law. It does. See footnote 1, *supra,* p. 1.

It should be noted that the federal statute and rule here in question specifically proscribe fraud. This distinguishes it from the federal statute involved in *Montana-Dakota Utilities Company* v. *Northwestern Public Service Company,* 341 U. S. 246, upon which both petitioner and respondents rely. In *Montana,* this Court held that the mere claim of a remedy under a federal statute, based on fraud, where the statute did not proscribe fraud, gave federal jurisdiction even though on the merits such claim was invalid. Respondents' discussion of this case (Br. 10) exhibits the confusion between jurisdiction and merits against which Mr. Justice Jackson warned, 341 U. S., at p. 249.

2. After conceding that the wrong charged in *Bell* v. *Hood* was a violation of both state and federal law, respondents seek to distinguish the case as follows (Br. 11):

> "Accordingly, Mr. Justice Black pointed out that the violations of the Constitution alleged there formed 'the sole basis of the relief sought' (327 U. S. 683). The cases cited by petitioner (Petition, p. 12), viz., *Fitzgerald* v. *Pan-American World Airways,* 229 F. 2d 499 (2d Cir., 1956), and *Fielding* v. *Allen,* 181 F. 2d 163 (2d Cir.,

1950), were applications of the doctrine of *Bell* v. *Hood.*"

Apparently respondents mean by the above that federal jurisdiction is sustained in cases where the wrong complained of violates both state and federal law only if plaintiff asserts, contrary to the fact, that the federal wrong is "the sole basis of the relief sought". Such a contention not only violates all reason but is contrary to *Hurn* v. *Oursler, supra,* where plaintiff expressly relied on both state and federal law and was allowed to assert on the merits his state-law grounds when the federal grounds were determined to be without merit.

As appears from the context, the phrase quoted by Mr. Justice Black in *Bell* v. *Hood,* 327 U. S. 678, 681, that "the party who brings a suit is master to decide what law he will rely upon" means simply that plaintiff must say that he relies on federal law in order to get into a federal court. It does not mean that once there he must disclaim all reliance on state law. *Hurn* v. *Oursler, supra.* Indeed, in *Bell, Fitzgerald* and *Fielding,* which respondents cite, it was quite clear that plaintiff's complaint was based on state-law grounds as well as federal grounds; in every case it was urged that this was a reason for denying federal jurisdiction; and in every case it was held that the mere presence of state-law grounds was quite immaterial to federal jurisdiction.

II

Respondents seek to excuse the failure of the Court of Appeals to decide the question of laches seasonably raised and presented by asserting (Br. 14), "The Court of Appeals properly refrained from passing on the rights secured to stockholders, individually or representatively, by Section 14(a), since the point was not before it."

This statement is inaccurate.

The District Court held (1) that an individual or representative action lay to vindicate the violation of the federal statute; (2) that such an action had not been brought; (3) that he would grant leave to amend to bring it, (4) except for the fact that such an action was barred by laches. Respondents do not deny that the last holding was error, or that the Court of Appeals refused to review that error. They assert only that the error was raised "belatedly" by request for leave to amend on petition for rehearing in the Court of Appeals. (Br. 14)

Petitioner has consistently asserted that he did not need leave to amend and, in the alternative, that if he did need it he had it from the District Court. His original brief on appeal clearly pointed out the error which the Court of Appeals refused to review.[3] The

[3] The pertinent provisions of petitioner's Main Brief in the Court of Appeals appear at pp. 5, 6 (footnote) and 22-24. The pertinent provisions in the petition for rehearing are copied at pp. 30-34 of the petition for certiorari.

error was elementary; it was not denied; and the probable reason why the Court fell into this error is stated in our petition, pp. 15-16, and is not disputed.

It is significant that respondents do not deny that if, as we assert, the Court of Appeals failed and refused to review the plain error of the District Court on the point of laches, this action constitutes such a departure from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision.

Respectfully submitted,

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